

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

PERIODIC REPORTING
(PROPOSAL TWO)

Docket No. RM2021-4

REPLY COMMENTS OF THE UNITED STATES POSTAL SERVICE
REGARDING PROPOSAL TWO
(May 25, 2021)

On May 14, 2021, pursuant to Order No. 5852 (March 26, 2021), four sets of initial comments were filed regarding Proposal Two. Those were submitted by the Public Representative (PR), the Association for Postal Commerce (PostCom), Pitney Bowes (PB), and an aggregation of trade associations – National Postal Policy Council, Major Mailers Association, National Association of Presort Mailers, and the Associations for Mail Electronic Enhancement (NPPC). All four sets of comments make arguments against at least one aspect of Proposal Two. The Postal Service hereby submits its reply to those arguments.¹

As explained below, the merits of Proposal Two are sound, and the criticisms advanced by the commenters offer no valid basis for rejection of the proposal. The claims of equivalences between Proposal Two and previous dockets do not withstand scrutiny. Proposal Two corrects the classification of all allied costs, carefully separating those that are influenced by actions necessary for presortation from those that are not so influenced. Commenters, by failing to acknowledge the differences, and by failing to

¹ A separate Motion for Leave to file reply comments is being submitted concurrently with this pleading.

acknowledge that several pools are actually proposed to be reclassified from “Fixed” to influenced by presort, mischaracterize the proposal. Alleged failure to adhere to methodological contrivance imagined by the commenters provide no reasonable grounds to reject the proposal. Moreover, several commenters – although not the Public Representative -- insist on retaining an inferior P.O. Box distribution cost methodology that is neither necessary nor accurate. The proposal should be judged on its actual merits, and not the commenters’ mischaracterizations.

1. The Public Representative, Pitney Bowes, and NPPC wrongly frame Proposal Two as identical to rejected proposals in previous dockets.

On page 1 of its comments Pitney Bowes argues that:

The Commission should reject Proposal Two because it is largely based on arguments the Commission has previously considered and rejected.

Similarly, the PR Comments at page 3 claim that the Postal Service “provides no new rationale compared with previous dockets where it tried to persuade the Commission to treat allied costs as fixed with respect to presort.” Likewise, NPPC argues:

The Commission has twice previously rejected proposals very similar to those the Postal Service is making in this proceeding, most recently in Order No. 1320, resolving Docket No. R2010-13. (NPPC Comments at 1.)

NPPC goes on to recount at length the Commission’s rejection in Docket No. RM2010-13 of the Postal Service’s proposal to treat non-modeled cost pools as fixed with respect to presort level by default. NPPC Comments at 2-4. Commenters inappropriately conflate the proposed reclassification of specific cost pools (where the Postal Service’s analysis shows cost avoidances to be associated with drop-shipping rather than presorting) with the entirety of Proposal Two. The incorrect implication is

that Proposal Two broadly seeks to reclassify allied labor cost pools that are currently piggybacked (or Correlated in Proposal Two terms) in the Commission's accepted methodology to the Unrelated category. In fact, Proposal Two neither posits a default treatment for any non-modeled cost pool nor does it seek only to reclassify piggybacked cost pools to Unrelated.

As the Postal Service has described in the proposal and ChIR responses, Proposal Two comprehensively reviewed cost pool classifications in light of changes to mail processing cost pools since Docket No. RM2010-1. Some of the proposed changes to cost pool classifications represent cases where, for various reasons, the Proposal Two would harmonize the treatment of logically similar cost pools that are classified inconsistently in the currently accepted model. These include:

- Inconsistent classification of manual allied labor operations performing tray separation or tray sorting—MODS opening and pouching cost pools,² currently treated as fixed—and corresponding automated tray sorting operations, currently treated as piggybacked. Proposal Two accepts the logic that costs in these operations can in principle depend on presort depth, and would reclassify the manual allied labor operations to piggybacked (Correlated), consistent with the treatment of automated tray sorting.
Response to ChIR No. 3, question 5.
- Inconsistent classification of Business Reply Mail operations between MODS and non-MODS facilities, where the corresponding non-MODS cost pool was

² MODS 1OPBULK, 1OPPREF, and 1POUCHNG.

introduced after the establishment of the current classification methodology.

Proposal Two harmonizes the treatment as Unrelated (Fixed), consistent with the accepted treatment of the MODS cost pool (which existed as of Docket No. R2006-1). Responses to ChIR No. 2, question 3(d) and ChIR No. 3, question 2.

Other proposed changes stem from review of the activities comprising the cost pools in question. For example, the proposed change to classify cost pools for MODS and non-MODS miscellaneous operations as fixed is based on review of the activities performed within the cost pools. MODS and IOCS data show that the primary mail processing activities in these cost pools relate to verification and destruction of undeliverable-as-addressed (UAA) waste mail. The proposed classification as fixed is consistent with individual presorted First-Class Mail letters reaching such UAA operations due to address quality and/or mailer preferences as to UAA handling, rather than presort depth. Response to ChIR No. 2, Question 3(a).

Finally, the proposed change to eliminate modeling of P.O. Box distribution costs and treat the associated cost pool as fixed is consistent with a previous proposed change that the Commission accepted. Petition at pages 6-7; response to ChIR No. 2, Question 3(d). Commenters offer no serious arguments why cases such as those described above should require extraordinary evidence to be resolved, let alone how preserving classification inconsistencies within the model would improve data quality relative to the relevant parts of Proposal Two.

2. The appropriate classification of platform operations and other cost pools treated as “Unrelated to Presort” in Proposal Two cost pools can be resolved without additional direct modeling

NPPC, Pitney Bowes, and PostCom contend that the Commission may reject Proposal Two solely because the proposal does not directly model the operations that would be treated as “Unrelated to Presort” under the proposal. Pitney Bowes Comments at 1; NPPC Comments at 5; PostCom comments at 2.

In suggesting the categorical rejection of Proposal Two for failure to develop model extensions, commenters largely fail to recognize the practical distinction between two types of cost pools. This first type consists of cost pools such as plant and NDC platform operations and the corresponding non-MODS allied labor operations (referenced below as platform and scanning operations),³ where there is unquestionably an active controversy as to the relative roles of presorting and drop-shipping in cost differences by rate category. The second type consists of other cost pools where, as discussed above, Proposal Two resolves classification inconsistencies or addresses operations that clearly have little role in the normal processing of presorted First-Class Mail letters. For the second type, the Commission should accept that it may be sufficient to clarify the nature of the work activities to justify changes, particularly in cases where modeling complexity would be great and the costs involved are small. For example, the complexity of developing and maintaining a model for UAA mailflows to the existing presort letter model structure would be far out of line with the need to resolve the disposition of 0.2 cents/piece of unit cost in the MODS and non-MODS

³ MODS 1PLATFRM, MODS 1SCAN, NDCs PLA, and non-MODS ALLIED.

miscellaneous cost pools.⁴ Establishing too high of a bar for changes could undesirably lead models to drift out of alignment with the Postal Service's evolving operations by making model maintenance excessively costly.

In the case of platform and scanning operations, commenters would have the Commission elevate the form of the proposal over its substance. Moreover, they would have the Commission insist upon development of a quantitative model to justify any changes to accepted methods for these cost pools despite the accepted methodology itself having originated with a "thought experiment"—as Pitney Bowes witness Buc put it in Docket No. R2006-1 (PB-T-2, revised October 26, 2006, at 14)—rather than an explicit mathematical model. Had the Commission applied the commenters' standard in Docket No. R2006-1, it never would have adopted witness Buc's proposal in the first place. The Postal Service does not suggest that it necessarily is wrong to accept changes based on sufficiently well-conceived thought experiments or other modeling approaches that do not quantify results. Rather, proposals should be resolved on their merits.

In Proposal Two, the Postal Service has explained at length how cost avoidances in platform and scanning arise due to mail entry (dropship) differences, rather than presort differences as such. See, e.g., Petition at 6-8; response to ChIR No. 3, question

⁴ In addition to the UAA activities noted above, the Postal Service observes that the MODS and non-MODS miscellaneous cost pools include a variety of other non-processing activities carried out by mail processing clerks, such as locking or unlocking facility doors and raising or lowering the U.S. flag. These costs are attributed to products because they are assigned IOCS activity codes that Commission methodology considers to be 100 percent volume-variable. It should be obvious that modeling door-locking and flag-raising activities would shed little light on their relationship to presorted First-Class Mail rate categories.

1(d). Commenters do not directly dispute that drop-shipping causes cost avoidances, but rather appeal—as witness Buc did in Docket No. R2006-1—to “correlations” between presort depth and platform costs. See, e.g., NPPC Comments at 6. The Postal Service does not dispute the existence of such correlations, which naturally arise as presorting to at least the AADC level (or greater) is a prerequisite for drop-shipping to destination AADCs. However, witness Buc’s original account and the Commission’s subsequent decisions all have elided the question of which activity—presorting or drop-shipping—causes the cost avoidances. The distinction is critical for developing First-Class Mai presort letter cost avoidances because mailers are eligible for presort discounts whether or not they also drop-ship their mail. This also forms a key distinction with the Docket No. RM2021-6 direct pallet discount cited by Pitney Bowes (PB Comments at 27), where the discount relates to additional preparation requirements that allow eligible pallets to avoid additional allied labor costs.

Pitney Bowes similarly attempts to conflate presort cost avoidances in distribution and non-platform allied labor operations with dropship cost avoidances arising in platform and scanning operations by drawing inappropriate connections between these operations’ distinct underlying patterns of cost causality. Pitney Bowes inappropriately cites current and past Postal Service modeling of mail processing operations for estimation of volume-variability factors in support of piggybacking platform costs on distribution operations’ costs. Pitney Bowes comments at 20-21. The cited testimony actually contends only that distribution volumes are potential “proxy” workload drivers for allied labor, and do not completely characterize volume drivers for allied operations: “[F]ully specified factor requirements models for allied labor operations could include

variables representing *several cost drivers in addition to the piece handling volumes* from sorting operations used by Dr. Bradley.” Docket No. R2000-1, USPS-T-15 at 137-138 (emphasis added). Pitney Bowes’ reference to the Postal Service’s econometric model for automated letter volume-variability, in pending Docket No. RM2020-13, also is silent on the question of the relationship between MODS TPF (which are avoided with presort) and allied labor cost pools that are outside the scope of the Docket No. RM2020-13 analysis.⁵ Pitney Bowes is similarly incautious in citing Commission findings with respect to allied operations that move mail within facilities and between distribution operations and the dock. Pitney Bowes Comments at 23. Many of those activities are part of non-platform allied labor cost pools (e.g., MODS 1OPPREF and 1DSPATCH, representing opening unit and dispatching operations) that Proposal Two classifies as Correlated (i.e., piggybacked). In opposition to the classification of non-MODS ALLIED as Unrelated to Presort, Pitney Bowes offers the irrelevant observation that more finely presorted pieces avoid some non-MODS manual distribution. Pitney Bowes comments at 25-26. This claim obfuscates the central question of how increased presort would allow pieces to avoid unloading at the destination post office in proportion to modeled cost differences, when presorted First-Class Mail letters overwhelmingly arrive in DPS trays regardless of presort level. As stated in the Petition at 7, these activities are “experienced by all pieces regardless of presort... when they exit the mail processing stream.”

⁵ Pitney Bowes here appears not to have appropriately distinguished some incidental allied labor activities that are part of the modeled MODS distribution cost pools, with other allied labor activities that are in stand-alone cost pools that are not modeled.

Pitney Bowes ultimately seeks to make a virtue of the blurring of presort and dropship cost avoidances as reflecting an “integral relationship.” Pitney Bowes Comments at 28. But from an ECPR perspective, combining presort and dropship effects is undesirable as it sends incorrect price signals for presorting. It would tend to generally over-value presorting activities by including cost savings arising from coincidental drop-shipping in the cost basis for the presort discounts. Additionally, combining presort and dropship avoidances effectively compensates non-dropshipping mailers for dropship activities they do not actually perform.

The “Simple Thought Experiment” presented on pages 30-32 of the Pitney Bowes Comments also depends critically on conflating presort and dropship effects on costs. Pitney Bowes suggests that it is unreasonable to expect allied labor costs to be invariant if all presorted First-Class letters converted to MAADC presort. The Postal Service does not necessarily disagree—in part because it also regards a number of allied labor cost pools as being appropriately treated as piggybacked (Correlated)—but notes that the actual allied labor cost response would depend critically on the resulting entry profile of the mail, which could change dramatically in such a scenario. However, Pitney Bowes’ thought experiment begs the question of why platform and scanning costs should increase proportionally to distribution costs for AADC and 5-Digit pieces that were entered at origin rather than destination facilities, and thus whose entry points would be hypothetically unchanged in such a scenario.

More generally, the Postal Service suggests that the probative value of the Pitney Bowes thought experiment is limited since the purpose of the models is to estimate the marginal cost changes of variations in presort holding non-presort

characteristics constant. In this light, the Postal Service submits that a more appropriate type of question is, how much should allied labor costs change if a piece upgrades from MAADC to AADC presort, or from AADC to 5-Digit presort, holding its entry point constant? Such a scenario is not a *reductio ad absurdum*, but rather the type of question the model seeks to answer. Proposal Two suggests that there would be cost avoidances in several allied labor cost pools (those treated as Correlated), where costs are caused in large part by movements to and among distribution operations within plants. However, platform and scanning cost avoidances would be negligible because, in this scenario, the presort upgrade alone would not allow pieces to avoid loading and unloading activities or activities related to inter-facility movements.

3. P.O. Box Costs are accurately measured without modeling

NPPC and Pitney Bowes both oppose the proposed elimination of P.O. Box distribution costs from the mailflow models and the treatment of the associated non-MODS costpool as Unrelated to Presort.⁶ NPPC Comments at 7-9, Pitney Bowes comments at 32-35. Both Commission precedent and the record in this proceeding support adoption of the proposed change. As the Commission previously found:

However, the extent to which a piece is workshared (or not) would not appear to affect the cost of distributing it to a post office box. Time Inc. has not explained why it should take more (or less) time to sort a flat to a post office box depending on how the piece is prepared and entered. It is unclear on this record whether the differences found by Time Inc. are due to mail characteristics related to worksharing or mail characteristics that are unrelated to worksharing (such as income of box holders). The Commission has devoted significant resources to analyzing this question. However, based on the record in this proceeding, the costs of sorting

⁶ The Public Representative supports this part of Proposal Two. PR Comments at 5.

mailing to post office boxes are properly treated as non-modeled, i.e., non-worksharing related. Order No. 1656 (Docket No. RM2012-8, February 14, 2013) at 17.

Both NPPC and Pitney Bowes seek to draw distinctions with Docket No. RM2012-8 based on the existence of DPS processing for letters. NPPC draws an analogy between carrier casing cost avoidances due to DPS and PO Box distribution costs. NPPC Comments at 8. This is inappropriate because, in contrast to DPS mail avoiding carrier casing entirely, mail sent to P.O. Boxes must ultimately be sorted into the boxes; DPS does not allow this activity to be avoided. Likewise, both parties suggest that changes to measured P.O. Box costs in the CRA are unexplained when, in fact, the Postal Service cited multiple methodological changes affecting both piggybacked and unpiggybacked P.O. Box costs. Response to ChIR No. 1, question 4(b)-(c).

For P.O. Box distribution, the existing explicit model (which dates to Docket No. MC95-1, prior to the widespread deployment of DPS) assumes that DPS letters can be sorted to boxes faster than non-DPS letters. As the Postal Service noted in response to ChIR No. 1, question 4(d), it believes that the assumed DPS P.O. Box productivity underlying the accepted model is clearly overstated given the prevalence of DPS in the current letter environment and the large difference between modeled and actual P.O. Box distribution costs. Nevertheless, the P.O. Box cost differences are small relative to the overall model cost differences: the model implies that the P.O. Box costs are essentially fixed. Pitney Bowes's own analysis shows that the model cost difference between Automation 5-Digit (0.189 cents) and automation MAADC letters (0.199 cents) is 5.3 percent (PB Comments at 32, Table 14). In contrast, the accepted model cost

difference between automation MAADC and 5-Digit is 341.6 percent (5.696 vs. 1.290 cents, see Docket No. ACR2020, USPS-FY20-10, “USPS-FY20-10 FCM Letters.xlsx,” worksheet “Presort Letters Sum”).

For the 23 billion Automation 5-Digit pieces, the model cost differential implies a cost avoidance relative to automation MAADC due to the DPS P.O. Box differential of \$2.5 million in aggregate. Inclusion of the P.O. Box pool in the CRA proportional adjustment factor increases the factor from 1.688 to 1.815, reflecting the model costs’ understatement of actual CRA costs in the non-MODS D.P.O. Box cost pool.

Mathematically, this has the effect of treating the P.O. Box modeling *error* as a cost avoidable with presorting, and thus greatly inflates the related cost avoidance. As a result, the 0.011 cent/piece model cost difference between automation MAADC and automation 5-Digit expands to an 0.436 cent difference in the worksharing-related unit costs after the application of the proportional adjustment – a 41-fold increase in the cost avoidance that implies 5-digit pieces addressed to P.O. Boxes avoid nearly \$100 million in costs beyond the model-based avoidance. See Table 1, below, as well as the Excel spreadsheet electronically attached these Reply Comments. Among other implausible implications, the cost differential owing to the proportional treatment of the non-MODS D.P.O. Box would suggest that 5-Digit pieces have a larger P.O. Box cost avoidance relative to automation MAADC than the *entire* P.O. Box distribution labor cost of single-piece First-Class Mail (\$84.6 million in FY2020; see Docket No. ACR2020, USPS-FY20-7, file USPS-FY20-7 part1.xlsx, worksheet “II-2. nonMODS”). There is neither a logical nor a model-based justification for such a magnitude of P.O. Box cost avoidance, and the Commission should adopt this part of Proposal Two.

Table 1. Excess P.O. Box Distribution Cost Avoidance due to Proportional Treatment of D. P.O. BOX Cost Pool

	Column	(1)	(2)	(3)	(4)
				Total WS Related Unit Cost (Cents)	
Row	Presort Level	Modeled P.O. Box Unit Cost (Cents)	Volume	P.O.Box Proportional	P.O. Box Fixed
(1)	Automation Mixed AADC	0.199	1,575,578,656	17.096	16.744
(2)	Automation AADC	0.195	7,524,739,336	14.299	14.124
(3)	Automation 5-Digit	0.189	23,417,356,641	10.189	10.272
(4)	MAADC-5D Unit Cost Difference	0.011		6.907	6.472

(5)	MAADC-5D Difference due to P.O. Box Proportional	0.436	R4C3-R4C4
(6)	Model Avoided P.O. Box Costs (5D vs. MAADC)	\$2,459,116	R4C1*R3C2
(7)	Adjusted Cost Avoidance with P.O. Box Proportional	\$102,009,888	R5*R3C2

Sources:

(C1) Pitney Bowes Reply Comments (May 14, 2021),

Table 14

(C2) USPS-FY20-10, USPS-FY20-10 FCM Letters.xlsx, worksheet

"Presort Letters Sum"

(C3) USPS-FY20-10, USPS-FY20-10 FCM

Letters.xlsx, worksheet "Summary"

(C4) USPS-FY20-10, USPS-FY20-10 FCM Letters.xlsx, worksheet "Summary" with non-MODS P.O. Box cost pool treated as 'fixed'

Conclusion

Proposal Two presents a number of novel issues that merit careful consideration regarding the specific relationship between activities in various cost pools and presortation. Comments that seek to color all aspects of Proposal Two as previously and correctly rejected by the Commission paint with far too broad of a brush. Each

component of Proposal Two should be evaluated on its own merits. On that basis, the Postal Service submits that each will be shown to be justified.

Wherefore, the Postal Service respectfully requests the Commission approve Proposal Two as submitted in this proceeding.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorney:

Eric P. Koetting

475 L'Enfant Plaza, S.W.
Washington, D.C. 20260-1137
eric.p.koetting@usps.gov
(202) 277-6333
May 25, 2021